IN THE INCOME TAX APPELLATE TRIBUNAL
MUMBAI 'D' BENCH, MUMBAI.

Before Shri B.R. Baskaran (AM) & Shri Pavan Kumar Gadale (JM)

I.T.A. No. 2756/Mum/2022 (A.Y. 2018-19)

Mangal Credit and Fincorp Ltd. 1701-1702, 17th Floor, A-Wing Lotus Corporate Park, Western Express Highway, Goregaon-E Mumbai-400 063. PAN : AAACT4015F	Vs.	DCIT, CC-1(1) Partishtha Bhavan M.K. Road Mumbai-400 020.
(Appellant)		(Respondent)

Assessee by	Shri Neelkanth Khandelwal
Department by	Smt. Mahita Nair
Date of Hearing	18.04.2023
Date of Pronouncement	24.04.2023

O R D E R

Per B.R.Baskaran (AM) :-

The assessee has filed this appeal challenging the order dated 22.10.2022 passed by the learned CIT(A)-47, Mumbai and it relates to A.Y. 2018-19. The assessee is aggrieved by the decision of the learned CIT(A) in confirming the addition of Rs. 1.50 crores made under section 56(2)(ix) of the I.T. Act.

2. The facts relating to the case are stated in brief. The assessee is non-banking financial company listed in Bombay Stock Exchange. The assessee had issued share warrants to ten persons @ Rs.36.45 per share. The assessee had allotted shares against share warrants issued to them upon payment of 25% of the value of shares. As per the terms of agreement, the balance amount has to be paid on 22.8.2017/2.9.2017 in order to fully convert the share warrants into shares, failing which the initial payment of 25% is liable to be forfeited. Out of the ten parties to whom share warrants were issued, six parties did not pay the balance amount of 75% and hence

the assessee forfeited the payments of 25% already made by them. The amount so forfeited worked out to Rs. 1,50,35,625/-. The AO noticed that the assessee did not offer the above said amount for taxation and hence the Assessing Officer proposed to assess the same as income of the assessee.

3. Before the Assessing Officer, the assessee contended that the amount so forfeited is a capital receipt in its hand and hence not liable to tax. In support of this contention, the assessee placed reliance on various case laws. However, the Assessing Officer took the view that the amount so forfeited by the assessee is liable to be taxed under section 56(2)(ix) of the Act. Accordingly he assessed the above said amount as income of the assessee under the above said section.

4. The learned CIT(A) also confirmed the same and hence the assessee has filed this appeal.

5. The Learned AR submitted that the provisions of section 56(2)(ix) of the Act shall have application only in respect of advance money received *in the course of transfer of the capital assets*, which was subsequently forfeited. He submitted that there should be transfer of capital asset; the assessee should have received advance in connection with transfer of said capital asset and the said advance should have been forfeited in order to get attracted by sec. 56(2)(ix) of the Act. He submitted that, in the instant case, the assessee did not receive money in course of transfer of capital assets, but received the same on issuing share capital. Accordingly, the Ld A.R submitted that the provisions of section 56(2)(ix) of the Act will not apply to the facts of the present case. He further submitted that the amount forfeited by the assessee shall constitute capital receipt and the same is not liable to tax. In support of his contention, the Learned AR placed reliance on the decision rendered by Delhi Bench of the Tribunal in the case of M/s. R.S. Triveni Foods P. Ltd. Vs. Addl. CIT (ITA No. 739/Del/2019 dated 5.8.2019). He submitted that the Delhi Bench of the Tribunal has considered an identical issue in the above

said case. However, in the case before Delhi bench of Tribunal, the assessee had issued fully convertible debentures and the part money collected was forfeited. The question that arose before the Tribunal was whether the provisions of section 56(2)(ix) of the Act will apply in respect of forfeited amount of application money collected on issuing fully convertible debentures. The Tribunal held that the provisions of sec.56(2)(ix) will not apply to the forfeited amount. Accordingly, the Ld A.R submitted that the ratio of the above said decision shall apply to the facts of present case also.

6. On the contrary, the learned DR supported the orders passed by the tax authorities. The learned DR also invited our attention to the Memorandum of Explaining the provisions of section 56(2)(ix) of the Act, when it was inserted by the Finance Act, 2014. The learned DR further submitted that the share capital shall qualify as "capital asset" and hence money forfeited by the assessee was in the nature of advance received during the course of transfer of capital asset falling within the scope of sec. 56(2)(ix) of the Act.

7. In the rejoinder, the Ld A.R submitted that the assessee has issued share warrants for raising capital and not in connection with the transfer of any asset belonging to the assessee. The shares issued by the assessee company may constitute capital asset in the hands of subscribers. What is relevant for the purpose of sec. 56(2)(ix) is that the assessee should have received advance amount in connection with the transfer of a capital asset, which is not the case here. Hence, the provisions of sec. 56(2)(ix) of the Act shall not apply.

8. We heard the rival contentions and perused the record. The fact remains that the assessee had received the impugned amount in connection with the issue of share capital and the same has been forfeited. The question that arises for adjudication is whether the amount so forfeited by the assessee from the share capital amount shall fall within the ambit of sec. 56(2)(ix) of

the Act or not? For this purpose, we extract below the provisions of sec.56(2)(ix) of the Act:-

> 56(2)(ix) any sum of money received as an advance or otherwise in the course of negotiations for transfer of a capital asset, if,—
> (a) such sum is forfeited; and
> (b) the negotiations do not result in transfer of such capital asset.

A careful reading of above said section would show that

(i) the money should have been received as an advance or otherwise

(ii) it should have been received in the course of negotiations for "transfer of a capital asset"

(iii) the said money should have been forfeited and

(iv) the negotiations did not result in transfer of capital asset

We notice on reading of the above said provision that, in order to attract the provisions of sec.56(2)(ix) of the Act, the advance money should have been received in the course of negotiations for "transfer of capital asset", meaning thereby "negotiation for transfer of capital asset" is an essential condition for invoking the provisions of sec.56(2)(ix). If the money has not been received in the course of negotiations for transfer of capital asset, then the provisions of sec.56(2)(ix) shall not apply.

9. In the instant case, the assessee has received money on issuing share capital in the form of exercise of rights in share warrants. The share capital so collected by the assessee is not in the course of negotiations for transfer of capital asset. The shares so issued may constitute Capital asset in the hands of the persons, who purchased the shares, but that is not relevant here. Issuing share capital does not result in transfer any capital asset. Accordingly, since the money was not received in the course of negotiations for transfer of capital asset, the provisions of sec.56(2)(ix) will not apply to the facts of the present case.

10. We notice that an identical view has been expressed by the Delhi bench of Tribunal in the case of M/s. R.S. Triveni Foods P. Ltd. Vs. Addl. CIT (supra). For the sake of convenience, we extract below the decision rendered by the Tribunal in the above cited case:-

> "11. We have heard the rival submissions, perused the relevant findings as well as material referred to before us. The main issue revolves around treating the amount of Rs. 3 crores by way of forfeiture of unsecured FCDs which though was treated as revenue receipt by the AO and held taxable as normal business income; however, the Ld. CIT(A) has taxed the same as income from other sources, by applying the deeming provision of section 56(2)(ix). As discussed above, the FCD's were allotted by the assessee company on 01.01.2014/03.01.2014, to two companies, 3,00,000/- debentures each with face value of Rs 100/-per FCD's by accepting the application money of Rs 50/- per debentures. As per the terms and conditions the FCD's, the FCD's were to carry interest @15% pa and were unsecured. The amount of Rs 50/- was payable as application money and balance Rs 50/- were payable within 90 days of allotment failing which the company had right to forfeiture. The debentures were fully convertible into equity shares of the company. Each debenture was to be allotted 8 equity shares of the company within 15 months from the date of allotment. During the year the call money received by the assessee company of Rs. 3,00,00,000/- was forfeited as the allottee companies despite various reminders and extension of time failed to submit the balance money and accordingly as per terms and conditions agreed the call money was forfeited.
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> 12. The Ld. AO disallowed the claim of the appellant and held that the said receipt is a revenue receipt and the forfeiture of the same does not change it characteristic as the capital receipt. The ground taken by the Ld AO was that the since the amount raised through allotment of debentures was utilized for acquisition of current assets and in view of the ratio of judgment in Logitronics Ltd. case, the above receipt were held to be of revenue nature. Ld. CIT(A) as stated above has changed the entire tenor of the addition, by holding that it is taxable as income from other sources u/s 56(2)(ix). Thus, the order of the AO stands merged with the order of the Ld. CIT(A) and therefore, we are only require to adjudicate, whether the said forfeiture of FCDs can be taxed u/s 56(2)(ix).
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> 13. In so far as the argument of the Ld. Counsel that the provision of section 56(2)(ix) would not be applicable on the facts of the present case because the said section has come w.e.f. 1.4.2015 and assessee has not received any sum or advance in this year, therefore, this provision would not be applicable. We are unable to subscribe to such an argument, because the deeming provision is attracted in the event when any sum is forfeited out of any sum and money received as advance or otherwise in the course of negotiations for the transfer of a capital assets. Here the factum of forfeiture of the FCDs has taken place in this year; therefore,

taxability qua the forfeiture amount has to be seen in this year. Such an argument of the Ld. Counsel, in our opinion is untenable.

14. From a plain reading of section 56(2)(ix), it is clear that the money should have been received as an advance or otherwise in the course of negotiation for a transfer of capital assets. Therefore, sum received in course of negotiation for transfer of a capital receipt (sic. Asset) is sine qua non for invoking of the deeming provision. The negotiation has to be in relation to transfer of a capital asset in whose hands the deeming provision is attracted. In other words, the capital asset which is the subject matter of negotiation for transfer must belong to the assessee. Ld. CIT (A) has referred to Explanation (d) below sub clause (vii) of Section 56(2), which defines capital asset to include 'shares and securities'. From bare reading of the said explanation it is seen that it is only applicable for the purpose of clause (vii) where an individual or HUF receives in any of the previous year from any person or persons any sum or money without consideration or any immovable property, etc. The said definition cannot be imported for purpose of interpreting a 'capital asset' in clause (ix). However, without going into this aspect, whether same definition is applicable in this clause or not, as it is not of much relevance. Here in this case, the assessee company has issued fully convertible 3,00,000 debentures to two companies, each with face value of Rs. 100/- per FCD and the application money was Rs. 50/- per debenture and balance Rs. 50/- was payable within 90 days of allotment, failing which the company had right to forfeit. "Debenture" is a long term debt instrument used by the companies to borrow money at a fixed rate of interest. It is a type of debt instrument which is not secured by any collateral. The debenture cannot be treated as a capital asset of the issuer company because it is a kind of debt instrument with an obligation to acknowledge the debt and pay interest. It is a capital asset in the hands of the person subscribing to the debenture or the allottee of the debenture, who is entitled to get interest at a stipulated rate and may also get right to equity shares if conditions of subscription prescribes so. The money received as advance as contemplated in section 56(2)(ix) means it should have been received during the course of negotiation for transfer of a capital asset, i.e., the capital asset of the issuer company and not the receiving company. The deeming provision is applicable in a situation where the person who owns a capital asset and enters into a negotiation for transfer of his capital asset with other person and receives certain advance which is forfeited on account of failure of negotiation of transfer of such capital asset, then money received as an advance is hit by the deeming provision which is taxable as income from other sources.

15. The aforesaid proposition is also borne out with the Legislative intent while introducing section 56(2)(ix) by Finance Act 2014, which is reproduced hereunder:-

Section 56 Finance Act, 2014

6.10 Taxability of advance for transfer of a capital asset where advance is forfeited (Sections 51 and 56) In Travencore Rubber & Tea Co. Ltd. v. CIT [2000] 243 ITR 158/109 Taxman 250 (SC) it was held that forfeiture of advance money received for transfer of capital asset cannot be treated as revenue receipt chargeable to tax. In order to overcome this ruling by the Supreme Court, section 56 relating to income from other sources has been amended by the Finance (No. 2) Act, 2014 by inserting a new clause (ix) in sub-section (2) of the aforesaid section. The said new clause (ix) provides that where any sum of money, received as an advance or otherwise in the course of the negotiations for transfer of a capital asset, is forfeited and the negotiations do not result in transfer of such capital asset, then, such sum shall be chargeable to income-tax under the head "Income from other sources". This amendment will take effect from 1st April, 2015 and will, accordingly, apply in relation to the assessment year 2015-16 and subsequent years.

Consequential amendments have been made to definition of 'income' in section 2(24) and in section 51. The existing provisions contained in clause (24) of section 2 define the term "income". The clause (24) has been amended so as to include any sum of money referred to in clause (ix) of sub-section (2) of section 56 in the definition of income. This amendment will take effect from 1st April, 2015 and will, accordingly, apply in relation to the assessment year 2015-16 and subsequent years.

The existing provisions contained in section 51 provide that where any capital asset was on any previous occasion the subject of negotiations for its transfer, any advance or other money received and retained by the assessee in respect of such negotiations shall be deducted from the cost for which the asset was acquired or the written down value or the fair market value, as the case may be, in computing the cost of acquisition. Finance (No. 2) Act, 2014 has inserted a proviso in the said section, so as to provide that where any sum of money received as an advance or otherwise in the course of the negotiations for transfer of a capital asset has been included in the total income of the assessee for any previous year in accordance with the provisions of clause (ix) of sub-section (2) of section 56, then, such sum shall not be deducted from the cost for which the asset was acquired or the written down value or the fair market value, as the case may be, in computing the cost of acquisition. This amendment aims to avoid double taxation of the forfeited advance. This amendment will take effect from 1st April, 2015 and will, accordingly, apply in relation to the assessment year 2015-16 and subsequent years.

[Emphasis in bold is ours] Thus, the aforesaid amendment has to be understood in light of section 51 of the Act, which provided that where any capital asset was on any previous occasion, subject matter of negotiations for its transfer and any advance or other money has been received and retained by the assessee in respect of such negotiations, then same was to be deducted from the cost for which the asset was acquired or the written down value or the fair market value, while computing the cost of acquisition. Now, from A.Y. 2015-16, if such sum received as an advance

is included in the total income then same is deducted from the cost of acquisition. Section 51 refers to capital asset belonging to the assessee which was a subject matter of negotiation for transfer and assessee receiving any sum as advance from such negotiation. It was not applicable to the transferee.

16. Here in this case the debentures were duly allotted to the subscribing companies and due to non payment of further call money under the agreement had led to the termination of the debentures and, therefore, said sum paid by the debenture holder cannot be held to be on account of transfer of capital asset in the hands of the assessee company. Debenture is debt instrument or is a kind of long term loan to borrow money at a fixed rate of interest. It is not a capital asset although the money raised by way of debenture becomes part of the issuer company's capital structure, but it does not become share capital. Thus, in our opinion, the forfeiture of the amount is not on account of failure of negotiation of transfer of capital asset of the assessee and thus, is not hit by section 56(2)(ix). The addition sustained by the Ld. CIT (A) is directed to be deleted."

11. In view of the foregoing discussions, we hold that the amount of Rs.1,50,35,625/- forfeited by the assessee out share capital issued by it shall not fall within the scope of sec.56(2)(ix) of the Act. Further, the said amount shall constitute a Capital receipt in the hands of the assessee. Accordingly, the above said amount is not taxable in the hands of the assessee. Accordingly, we set aside the order passed by Ld CIT(A) on this issue and direct the AO to delete the addition of the above said amount made in the hands of the assessee.

12. In the result, the appeal filed by the assessee is allowed.

Pronounced in the open court on 24.4.2023.

Sd/-	Sd/-
(PAVAN KUMAR GADALE)	(B.R. BASKARAN)
Judicial Member	Accountant Member

Mumbai; Dated : 24/04/2023

Copy of the Order forwarded to :

1. The Appellant
2. The Respondent
3. The CIT(Judicial)
4. PCIT

5. DR, ITAT, Mumbai
6. Guard File.

BY ORDER,

//True Copy//

(Assistant Registrar)
ITAT, Mumbai

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